

**BILL #** HCR 2002

**SPONSOR:** Anderson

**PREPARED BY:** Hans Olofsson

**TITLE:** property tax exemption; disabled veterans

**STATUS:** As Introduced

## FISCAL ANALYSIS

### Description

If approved by voters in the 2008 general election, this resolution would provide a property tax exemption for disabled veterans or their unmarried surviving spouses. The exemption would only apply to those veterans that are blind in both eyes, have lost the use of two or more limbs, or are classified as totally disabled by the U.S. Department of Veterans Affairs. The exemption would equal \$150,000 in full cash value for eligible veterans (or their surviving spouses) with household incomes of \$40,000 or less. For all other qualified veterans, the exemption would be limited to \$100,000 in full cash value.

### Estimated Impact

Conditional upon voter approval in November 2008, it is estimated that the General Fund will incur a cost not exceeding \$235,000 beginning in FY 2011. The bill will result in a reduction in statewide net assessed valuation (NAV), which will increase the state's K-12 education formula cost. That impact, however, may be offset by reduced costs for the automatic school tax rate reductions provided under the state's truth-in-taxation (TNT) statutes. If the TNT savings are incorporated, the bill will generate General Fund savings not exceeding \$(83,000) beginning in FY 2011.

For reasons described below, the estimates above only reflect the potential impact of the property tax exemption used by qualified disabled veterans, not their unmarried surviving spouses.

### Analysis

The Arizona Department of Veterans' Services (ADVS) estimates that about 1,200 disabled veterans would be eligible for the property tax exemption under this proposal. The number of unmarried surviving spouses of such veterans is unknown, but may be small. One reason for this is that the exemption would only apply to the surviving spouses of a small subset of disabled veterans, as defined in the bill (blind and 100% disabled veterans). In addition, for a surviving spouse to qualify for the exemption, the bill stipulates that her deceased disabled veteran spouse must have died "as a result of a service connected disease or injury." This suggests that any cause of death that was not related to prior military service (for example, accidents or non-military related ailments) would exclude the surviving spouse from the exemption. Additional information related to surviving spouses has been requested both from both ADVS and the U.S. Department of Veterans Affairs, but to date no such data has been provided.

As a result, this analysis assumes that the maximum number of properties that could potentially qualify for the exemption is 1,200. However, this figure may have to be revised later if additional data is furnished. An unknown number of potential exemptees are not homeowners and would, therefore, not be affected by the proposal. Using a homeownership rate of 68.2%, as provided by the U.S. Census Bureau, it is estimated that the number of eligible properties would be reduced to about 800. The exemption amounts applied to these properties would depend on the household incomes of the homeowners, as described above. Since the average full cash value of an owner-occupied residential parcel is currently more than \$210,000, it is further assumed that each qualified property owner would be able to use the full exemption amount allowed under the proposal.

HCR 2002 does not provide a definition of "household income," as such definitions are typically included in a separate companion bill, according to Legislative Council. (While tax exemptions are authorized by the constitution, they are often further defined by statutes.) For this reason, it is not clear whether the income measure under the proposal refers to adjusted gross income, as defined by the Department of Revenue (DOR), or some other alternative measure of income. For example, the household income measure used to determine eligibility for the property tax exemption to widows, widowers, and disabled persons does not include social security benefits and veterans disability pensions. This suggests that if a similar

income definition is used for this proposal, the effective or “real” income limit could be significantly higher than the nominal income limit of \$40,000 that applies to the \$150,000 property exemption. (To provide some perspective, ADVS estimates that totally disabled veterans receive an annual disability pension of slightly less than \$34,000. If this amount was not included under the definition of household income, the effective income limit would be increased to \$74,000.)

Because the income measure remains to be defined, it cannot be ruled out at this time that all 800 properties could potentially qualify for the \$150,000 exemption. For this reason, this assumption can be characterized as the “high end” estimate of the proposal. (It may be necessary to revise the estimate once household income has been defined under a separate bill.) Under this “high end” estimate, statewide full cash value would be reduced by \$120 million ( $= 800 \times \$150,000$ ). The corresponding primary NAV loss would be \$12 million ( $= \$120 \text{ million} \times 10\%$ ).

Under the Basic State Aid formula, the state pays for the cost of K-12 education not generated through local property taxes. The state also pays 40% (in FY 2011) of residential property taxes through the Arizona Department of Education (ADE) Homeowner’s Rebate program. By reducing NAV by \$12 million, the bill will result in a direct increase of the state share of K-12 funding by \$235,000. This includes the net impact of both Basic State Aid and the Homeowner’s Rebate.

This NAV reduction will also generate savings in the cost of the state’s TNT program. TNT reduces the school Qualifying Tax Rate (QTR) to offset growth in existing property values. This reduction occurs automatically unless the Legislature decides to forego the TNT adjustment. Under current law, the QTR is projected to be reduced by 6.9¢ in 2011, which will increase the state’s Basic State Aid cost. By reducing NAV, the legislation would result in the tax rate reduction being 0.1¢ less than projected, which would generate a TNT savings of \$318,000.

The fiscal impact of this bill is uncertain since the income measure used to determine the exemption amount is currently undefined, as noted above. The fiscal impact of this bill will also depend on whether the TNT impact is included. In the absence of a TNT adjustment, the net cost to the General Fund will be an estimated \$235,000. If the QTR is adjusted to account for TNT, however, the bill would have a General Fund savings of \$(83,000). This amount reflects the net impact of a \$235,000 increase in the state’s share of K-12 funding and a \$(318,000) savings from a lower than expected tax rate reduction.

### **Local Government Impact**

This bill may result in property tax losses for local governments and/or shifts of the tax burden to property owners not directly affected by this legislation.